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FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF SECRETARY

**EX PARTE**

William F. Caton  
Acting Secretary  
Federal Communications Commission  
Mail Stop 1170  
1919 M Street, N.W., Room 222  
Washington, D.C. 20554

Dear Mr. Caton:

DOCKET FILE COPY ORIGINAL

Re: CC Docket No. 94-1, Price Caps

Today, Dave Dorman, president of Pacific Bell, Peter Knight, and I met with Commissioner Ness and Jim Casserly of her staff, Richard Welch of Commissioner Chong's office, and Lauren Belvin of Commissioner Quello's office to discuss issues contained in the attached document which was used during the meeting. Please associate this material with the above-referenced proceeding.

We are submitting two copies of this notice in accordance with Section 1.1206(a)(1) of the Commission's Rules.

Please stamp and return the provided copy to confirm your receipt. Please contact me should you have any questions or require additional information concerning this matter.

Sincerely,



Attachment

cc: Commissioner Ness  
Jim Casserly  
Richard Welch  
Lauren Belvin

No. of Copies rec'd 021  
List A B C D E

## **PRICE CAPS MEANS REGULATING *PRICES* -- NOT EARNINGS**

- *LECs' Prices Are A Bargain Compared To IECs' Prices*
- *If The Commission Regulates Earnings, It Can't Ignore IECs' Earnings*

## **PROVIDE INCENTIVES IN PRICE CAPS SO LECS MAY CONTINUE BUILDING THE SUPERHIGHWAY**

- *Eliminate Sharing and Earnings Caps*
- *Don't Increase the Productivity Factor*
- *Permit Additional Pricing Flexibility*

## **"ONE SIZE" REGULATION DOESN'T FIT ALL MARKETS**

- *Access Services -- not Local Exchange Services -- are Regulated by Price Caps*
- *California Has Extremely Dense Concentrations Of Volumes And Revenues In Small Geographic Areas*
- *The Rules Generally Permit "One-Size" Pricing despite Enormous Differences in Costs by Geography and Density*

## **COMPETITION DOESN'T STAND STILL. NEITHER SHOULD REGULATION**

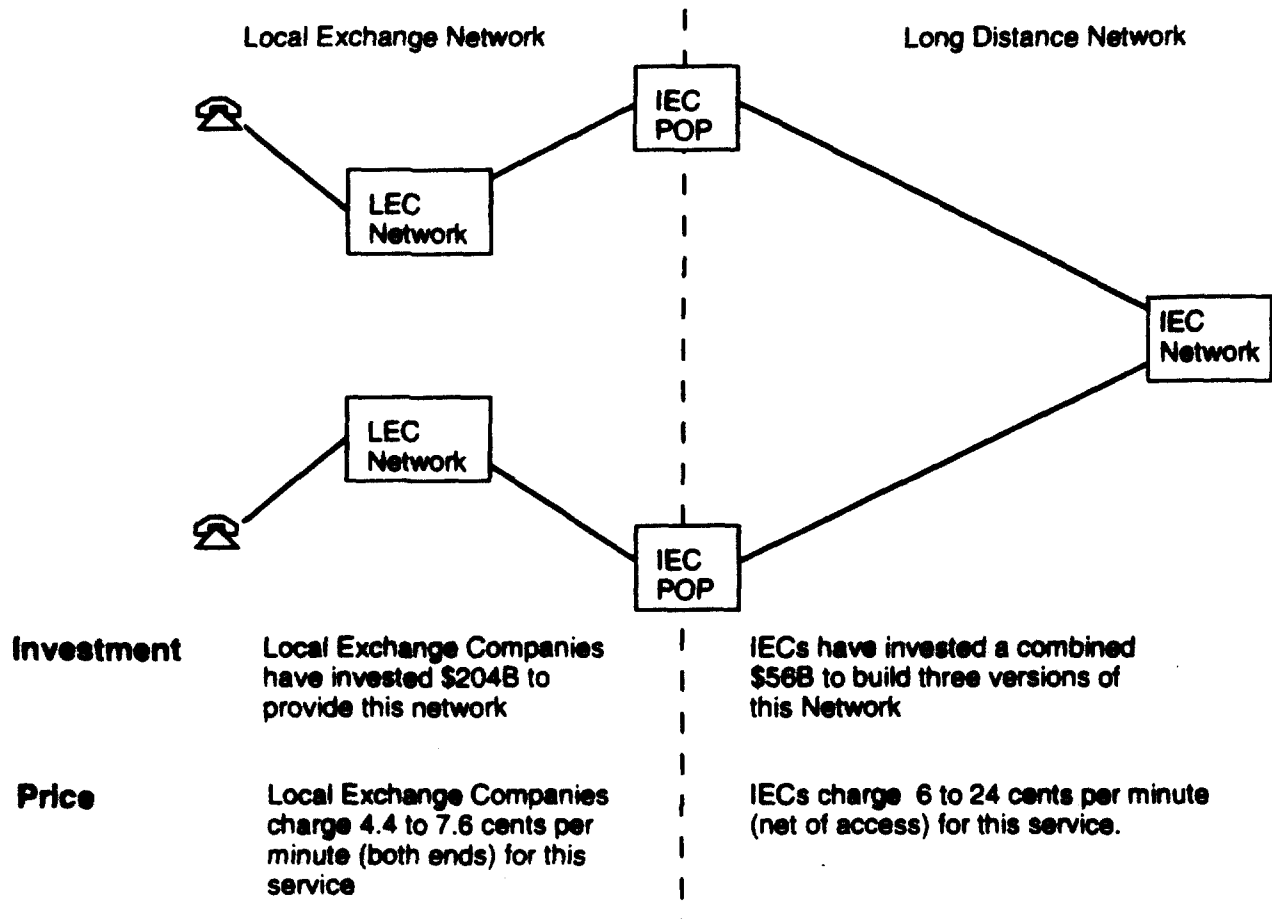
- *An Adaptive form of Regulation is Needed to Ensure that Consumers Benefit*
- *To Be Fair And Efficient, Regulators Should Treat All Providers In A Competitive Market Alike*

## **WE ARE A LEADER IN HELPING EDUCATION MEET ITS COMMUNICATION NEEDS.**

- *Our Education First Program To "Wire" approximately 8,600 Schools And Libraries Will Cost Up To \$115M*
- *We Have Requested Permission From Our State Commission To Offer A "Knowledge Network ISDN" Service For Schools And Libraries*

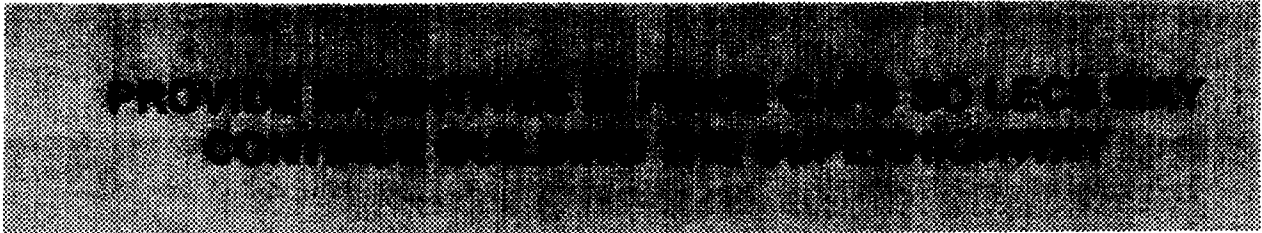


- **LECs' prices are a bargain compared to IECs' prices**



- **If the Commission regulates earnings, it can't ignore IECs' earnings.**

<u>Year</u>	<u>Pacific Bell Interstate ROR As Filed</u>	<u>AT&amp;T Interstate ROR As Filed</u>	<u>Pacific Bell Interstate ROR Using AT&amp;T Depreciation</u>
1991	11.85%	13.41%	8.18%
1992	12.68%	12.77%	9.24%
1993	12.85%	13.49%	9.41%



- **Eliminate Sharing and Earnings Caps**

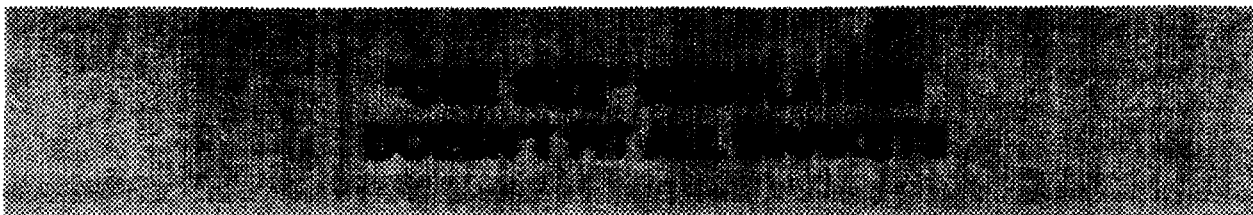
- *Promotes infrastructure development*
- *Retains fruits of our labor rather than giving them to our competitors*
- *Eliminates the need for arbitrary cost allocations and reduces concerns of cross subsidy*

- **Don't Increase the Productivity Factor**

- *Productivity calculated from LECs' earnings is rate of return in sheep's clothing.*
- *The productivity factor should be calculated from national data by impartial economists*
- *A five-year rolling average of total factor productivity will incorporate changes in technology and competition*

- **Permit Additional Pricing Flexibility**

- *Increase annual downward pricing flexibility to 15% for all pricing bands and zones*
- *Include cross elastic services in the same pricing bands*



- **Access Services – not Local Exchange Services – are Regulated by Price Caps**

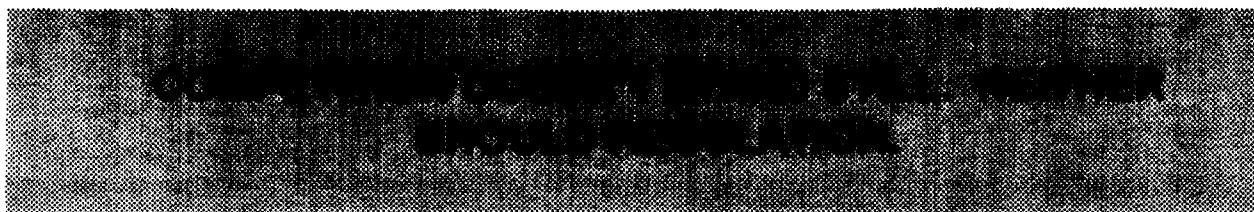
- *The level of competition in local exchange markets is independent of that in access markets and is not indicative of whether access markets are competitive*
- *The relevant markets to measure to estimate the level of access competition are small and geographically discrete areas*
- *In California, the majority of customers are located in access markets that have competitive alternatives*

- **California Has Extremely Dense Concentrations Of Volumes And Revenues In Small Geographic Areas (See Appendix For Data)**

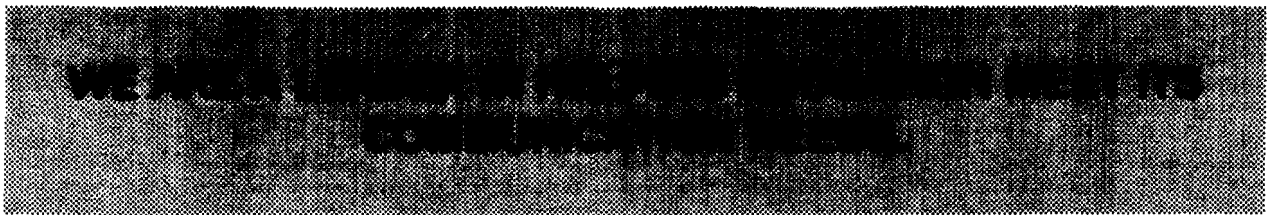
- *This encourages competitors to construct facilities and target customers in our most lucrative markets with minimal capital outlays*
- *Cream skimming by competitors reduces the subsidy needed to cover services priced below economic cost*

- **The Rules Generally Permit “One-Size” Pricing despite Enormous Differences in Costs by Geography and Density**

- *Our prices still reflect arbitrary cost allocations embedded years ago to achieve public policy goals. Today these allocations compromise our ability to compete.*
- *We must price most services under the false pretext that California is a single homogenous market where customers have no alternatives – so some customers pay too much and others pay too little.*

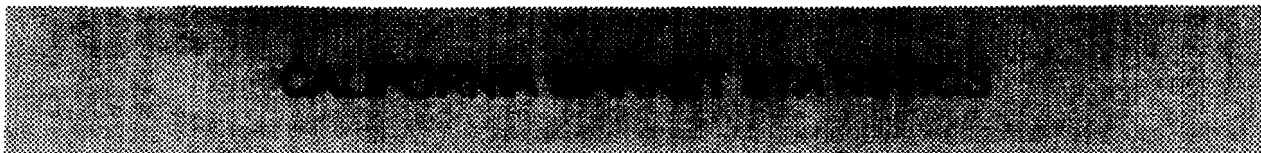


- **An Adaptive Form Of Regulation Is Needed To Ensure That Consumers Benefit**
  - *Although our competitors have benefited from the Commission's pro-competitive policies – interconnection, collocation – consumers haven't*
  - *The degree of regulation in a market should correspond to the level of access competition in that market*
  - *Effective regulation should make competitors address market realities – current regulation enables them to take advantage of regulatory artifice*
  
- **To Be Fair And Efficient, Regulators Should Treat All Providers In A Competitive Market Alike**
  - *Eliminate vestiges of rate of return regulation – sharing, productivity and earnings caps*
  - *Require all competitors to file service maps and other data necessary to analyze the degree of competition in access markets*
  - *Issue an FNPRM to design an adaptive framework for price cap regulation*



- **Our Education First Program To "Wire" Approximately 8,600 Schools And Libraries Will Cost Up To \$115M**
  - *It will provide*
    - *Free installation for up to 4 ISDN lines (including interactive telelearning)*
    - *Inside wiring for up to 2 locations per site*
    - *1 additional ISDN line and associated inside wiring to connect individual school sites with a school hub location*
    - *Free usage and monthly service for 1 year*
- **We Have Requested Permission From Our State Commission To Offer A "Knowledge Network ISDN" Service For Schools And Libraries**
  - *Reduced rates for these educational institutions for subsequent years*
    - *A flat monthly rate including message charges*





- **California has extremely dense concentrations of volumes and revenues in small geographic areas**
  - *75% of our access minutes and 67% of our access revenues come from our four major metro areas (San Francisco, Los Angeles, Sacramento and San Diego)*
  - *90% of our interstate hicap circuits are located in 12% of our wire centers*
  - *33% of our interstate access minutes come from only 8% of our wire centers*
  - *96% of the traffic in downtown San Francisco is currently addressable by existing CAP facilities*
- **California's market characteristics encourage competitors to construct facilities and target customers in our most lucrative markets with minimal capital outlays**
  - *Collocators currently have 70 cages located in 46 of our key wire centers and can access 70% of our transport services*
  - *CAPs currently have thousands of miles of excess fiber capacity for customers to use in place of our network*